# How to Get a Small Business Loan (Updated 2019) – The Ultimate Guide

*By Daniel Lewis*

| March 13, 2019

1

# An Introduction to Small Business Loans

Getting a business loan is an art that needs to be carefully researched in order to get right. There are so many options that it can be very easy to make the wrong decision. **Pinning all of your dreams on a 3-month loan application that gets rejected could have catastrophic consequences for your new enterprise.** Thankfully, there are some well-trodden paths that you can follow in order to acquire the right business loan.

Table of Contents

# Getting a Small Business Loan

The first step in getting a business loan is figuring out exactly what you need it for. For a new business, this is often obvious, in that you need the funds to expand. However, it is also helpful to understand what you are going to spend the money on with as much precision as possible.

Figuring out that you need a loan is the easy part. **The next step is to pinpoint what kind of loan you are looking for and how best to apply for it**. It is also helpful to understand how the loan process works and some statistics about the industry. For example:

1. About 1 in 6 small business loan applications are rejected.
2. Businesses in certain industries have a large approval rating, others have a large failure rate.
3. Banks are the most common place that companies go to get a loan. However, the approval rates by banks are far smaller than the approval rates from alternative lenders.

# An Overview of The Different Loan Types

The most common type of loan is the business term loan, which is a loan provided to a business for a specific length. Typically, short-term loans are between 3 to 12 months, medium-term loans are between 1 and 5 years, and long term loans are anything beyond 5 years. The SBA(7)(a) is an example of a term loan, as the typical loan type with favorable terms and an incredibly difficult approval process. But there are a wide number of alternative loan options available with varying conditions.

- **Online Term Loan** – This is a term loan with an online lender that will have much lower requirements and an easier approval process. The only real disadvantage is that the APR will be higher. For example, Kabbage offers term loans with minimum requirements of a credit score of 560 and annual revenue of at least $50,000. Ondeck requires a credit score of 600 and annual revenue of at least $100,000. Once these (and a few other) requirements are met, funding is generally quick and painless.
- **Business Lines of Credit** – A business line of credit (LOC) offers more flexibility than conventional term loans. This is because you can simply withdraw a set amount each day and pay interest only on what you borrow. Typically, business lines of credit are a little more difficult to qualify for in comparison to term loans. You can use this line of credit as often or as little as you like, so it is something of a gold standard in the loan industry. However, the APR can be high, much like using a credit card.
- **Merchant Cash Advance** – The merchant cash advance (MCA) is often considered a financial option of last resort. The total cost and the daily repayment schedule can be huge. The MCA offers an upfront sum in return for a cut of future transactions, using a percentage of credit card sales until the advance is paid. The lump sum and interest are usually paid daily or weekly. The factor rate is typically between 1.2 and 1.5. This means that if you were advanced $100,000 you would be paying back $120,000 – $150,000.
- **Property Loans** – Property loans or equipment financing is where you borrow a loan specifically for the purchase of equipment. They are typically easier to obtain and require less paperwork. For this reason, you should take out an equipment financing loan separately so the total term loan amount you need is lower and easier to acquire. Equipment financing can typically include machinery, cars, and computers.
- **Invoice Factoring, Financing & Discounting**– Sometimes, there is a delay between invoicing and payment that may not suit your business needs. Invoice factoring is a short-term financing option where you sell your invoices to a third party in return for payment. You do not get the full value of the invoices. The benefits of this are that you will gain immediate payment and do not have to chase your clients. Invoice factoring is sometimes called Accounts Receivable Financing (ARF). **Invoice discounting is similar to invoice factoring**. But you will still have control of the sales ledger as opposed to invoice factoring. Invoice discounting is riskier for the lender as they do not have control over the invoice collection process and do not have contact with debtors. As such, invoice discounting is typically only offered to businesses that are more established.

There are many different kinds of loan option available and many permutations of the loans above. There are also other options such as trade finance, equity crowdfunding, peer-to-peer loans, and lease financing. **Remember to investigate the terms and conditions of your loan clearly**. **Additionally, remember to avoid payday loans, which are just short-term loans borrower against your next paycheck. They have notoriously high rates and are something of a predatory practice.**

Advance fee loans, where you pay an upfront fee to obtain the loan, are nearly always scams. There is no reason for this fee and the lender typically disappears once the fee has been paid. However, many institutions can charge a fee for processing a loan application, though this is seldom seen with online lenders.

# Questions to Ask Before Applying for a Loan

There are 5 major questions you will need to ask before applying for a business loan. These are:

(i) What are my chances of approval for this loan?

(ii) What amount of money do I require for my business?

(ii) How quickly do I need the capital?

(iv) What rate am I willing to pay on the funds?

(iv) What is the repayment schedule?

**These questions will tell you what avenue you will need to take. Do not apply for a loan if you have a low chance of qualifying. It will take up considerable time and resources, especially for bank loans which will require an onerous amount of documentation. The biggest mistake that applicants make is that they apply for the wrong type of loan and do not have a clear map of what the funds are needed for.**

# Determining Your Eligibility

Determining your eligibility will require many of the same questions as above. You will need to examine whether or not you are suitable for the loan by checking the credit score requirements, minimum annual revenue, and obviously the rate you are paying on the loan.

Lenders will also have requirements in relation to how long you have been in business, with 6 months being a minimum and sometimes 12 months. There may also be additional requirements, such as at least 3 months of activity in a checking account. You will have to check with each individual lender. But common qualifying criteria typically includes:

- Minimum credit score (500 – 600)
- Minimum time in business (3-12 months)
- Minimum annual revenue ($50,000 – $100,000)
- Activity in a business checking account (3-12 months)
- Eligible industry (certain industries, like charity and gambling, are not eligible for loans)

# Understanding and Raising Your Credit Score

There are a few things to understand about owning and raising a credit score. Many business owners do not actually know that they have a personal score as well as a business credit score, both being distinctly separate.

If your business is very small with no significant credit history, then the lenders will take your personal credit score as the business credit score for the purposes of the application. This is the case for both alternative lenders and banks.

**Business owners who understand their credit scores are more likely to get a loan. As per the Small Business American Dream survey, those with an understanding of their credit score are 41% more likely to get a loan. The survey also revealed some surprising facts about the loan application process. 23% of rejected applications do not know why they were turned down, 45% of owners do not even know they have a business credit score, and 82% don't know how to interpret their score.**

There are no real major tips for raising credit score. It just involves taking out loans and always paying them off on time. With a little patience, your credit score will raise. If you do not have a stellar credit rating, then select an appropriate loan that you can get right now. After a year or two, your credit rating will rise and you can get a loan with more

competitive interest rates. Just set reminders, be responsible, and pay your debts on time each month.

## Credit Scores – Things to Avoid

While raising a credit score is actually straightforward (but time-consuming), there are some definite items you need to avoid. There are many commonly accepted pieces of wisdom found online in relation to raising a credit score, which goes directly against the

official advice from the credit agencies themselves.

For example, **it is not a good idea to move debt around or to close unused credit cards as a means of artificially raising a credit score**. This may have the opposite effect. Additionally, it is better to keep outstanding balances low on revolving lines of credit such as credit cards. High outstanding debt is a black mark against your rating and is definitely something to be worked on.

You can re-establish your credit history by opening new accounts, just remember not to open too many accounts at once. One of the most important items to attend to in terms of raising your credit score is in disputing errors on your report – these occur far more often than you might think.

## Finding an Appropriate Lender For Your Industry

If possible, it can be more useful to find a lender who is experienced in your specific industry. Consider that there are different vastly different financing requirements within the restaurant industry, the IT industry, and the construction industry.

**The type of industry you are in can also determine the kind of financing that you need**. For example, in the construction industry, invoice factoring is ideal as it provides immediate payment for invoices where payment can be slow. Companies in the tourism industry will also need some kind of financing to cover them in the slow season, and a business line of credit might be appropriate, where funds are drawn and repaid as needed.

# Typical Short v Long Term Loan Requirements

**Short term loan requirements are quite easy to satisfy with far less documentation required.** With Ondeck, for example, the application process can be completed in as little as 10 minutes with funding supplied in less than 24 hours. For a short term loan, you will typically need to supply –

- Name
- Address
- Business Revenue
- Amount Needed

Many online applications require no documentation whatsoever. The supplied information is checked online using a proprietary algorithm which determines the risk levels and authenticity of the application.

**For a long term loan application, the requirements are often more onerous and are frequently underwritten by banks and large financial institutions**. An enormous amount of documentation is often a prerequisite. You will need to prepare well in advance and even with a strong application you could easily be rejected. The full list of required documentation for a typical SBA(7)(a) small business loan is listed here. It includes:

- A business debt schedule.
- A personal finance statement.
- A third-party business valuation.

- A draft loan authorization.
- A lenders credit memo.
- Income and balance sheet statement (along with many more financial documents).
- Real estate appraisals.
- License and franchise agreements.

Many of these documents can take a long time to acquire. So if you are pursuing an SBA(7)(a) loan, then you really need to be proactive and try to obtain all of the documentation in advance.

But before you go ahead and start collecting the documentation, remember that you need to check your eligibility first.

# Tips for a Successful Loan Application

**Lenders do not like inconsistent cash flow. So it is better to have a steady stream of monthly income each month than it is to have a number of once-off payments. If you do have lump payments, you can break it up so that weekly amounts flow into your business checking account. Psychologically, having a consistent flow of income indicates organization and consistency, which is exactly what lenders are**

**looking for.**

There are a number of industries not serviced by either banks or alternative lenders. This is because regulation prevents the facilitation of finance to businesses involved in certain activities. These include consumer and marketing cooperatives, dealers of stamps and rare coins, gambling, gaming, illegal firms, government-owned organizations, lending firms, loan packaging firms, non-profits, charitable organizations, real estate investment firms, pyramid schemes, multi-level marketing schemes, and multi sales distribution. These industries are largely considered either illegal, speculative, risky, or representative of a conflict of interest if the loan was generated.

**Remember to apply for a loan before you get into trouble**. When your finances are not the best, [then you won’t get approved for anything](). Another tip is to be frugal and

careful with your finances early on. Startups and small businesses need to focus more on doing things correctly over time as opposed to blowing budgets on marketing materials and inventory. A good accounting team or financial automation tool can help to get your business in order for the loan application.

**Focus on saving 3 months of capital first before expansion. It is a good way to build up a good credit score and also have capital saved for a rainy day. The most common cause of startup failure is premature scaling, meaning that they spend their money in the wrong places in an attempt to expand before they are ready to do so. The focus should be on capital acquisition first and spending on opportunities as they arise. Time and patience are very important and the ultimate purpose of businesses is wealth acquisition.**

# Traits That Lenders Look For

Lenders want to make money, just like anybody else. So they want to make sure that you are reliable enough so that there will see a return on their investment. Not only do they need to see a return, but they also need to turn a profit.

**The one trait that a lender looks for is organization. You need to show that you are organized across all possible dimensions of your business. This will demonstrate that you are consistent and can be relied upon to a large degree.**

If you do manage to get all of the required documentation for an SBA(7)(a), have a solid business plan, significant annual revenue, and a good credit score, then that shows that you are organized and dedicated to running a good business. The requirements may seem onerous, but they only want reputable applicants. Diligence, organization, and attention to detail are viewed upon far more favorably by lending institutions than creativity

or passion. They don’t make any more money when you have an excellent business model. But they will lose their investment if you go bankrupt.

**If you want to impress the lenders then try to get a good credit rating and draft an up-to-date business plan with appropriate financial forecasting. Along with the documentation, these two things will stand you in good stead for the bank loan application. It is also a good idea to stay informed with regard to the daily management of your finances. Review your costs, manage projections, be diligent with invoicing, and keep track of expenses.**

If you are convinced that you have an excellent idea and need money and expertise fast, then venture capital is an option. However, you have to be prepared to give up equity in your company. If it’s truly a good idea, the capitalists will want a significant stake to part with their money. For most small business owners, an alternative lending platform is the best possible option.


Online lenders have proliferated in the market in the past decade. This rise can be partially attributed due to the strict credit requirements of financial institutions and the general difficulty of acquiring funds. While large institutions still make up the larger share of total loans, this statistic is a little misleading. Banks get all of the biggest loans which can skew the figures. Many businesses are getting loans for smaller amounts from alternative lenders, which is leveling the playing field.

**It is important to keep in mind that online lenders are not a panacea for financial woes.** Business owners still need to pay their debts on time and they need to manage all aspects of the business process. But there are now more options available and people with a good idea and appropriate levels of business acumen can get the financing that

they need from a variety of different lenders. The most well-known of them with the associated requirements include:

1. **Fundbox** – 3 months in business with a minimum annual revenue of $50,000 and no minimum credit requirements. Amounts range up to $100,000 and they also offer invoice financing as well as terms loans and lines of credit. Funding is as quick as the next business day.
2. **Ondeck** – One year in business and $100,000 in annual revenue. Credit score of 500 for terms loans and 600 for business lines of credit. Applicant must have no bankruptcies during the past two years. APR ranges from 9% – 99% for term loans and 14% – 40% for lines of credit.
3. **Kabbage** – One year in business, $50,000 in revenue and a minimum credit score of 560. Amounts range from $2,000 – $250,000. Applicants must also have a business checking account or online payment account. The application process takes less than 10 minutes and no documents are required. APR ranges from 24% – 99%.
4. **Lending Club** – To qualify for a lending club loan, you need 12 months in business, $50,000 in annual revenue, and "at least fair or better personal credit". Applicants must also have no recent bankruptcies. Total amounts range from $5,000 to $300,000.

**Need more options before you choose your small business loan? Check out this list**

# Most Common Reasons Loans are Denied

Understanding the most common reasons why loans are denied can also help to secure a small business loan. Realistically, there are many reasons why a particular application may not succeed in the loan process, despite undertaking significant research. It is at the discretion of the lending institution whether to grant a loan or not. Above all, as mentioned at the start of this guide, **be clear why you need the loan and what you intend to use the funds for.** According to James Walter, the founder of loan platform BBC Easy –

*"In my prior experience as the co-founder of a lending company, one of the most basic errors made by loan applicants was not telling me why their company needs the money. And they wouldn't reveal why we should approve the loan even though their company doesn't meet our minimum standards"*

Lack of collateral is another significant reason that small businesses are denied funding. While this is not a problem for larger institutions, it can present difficulties for startups. Without collateral, lending institutions have little recourse in the event of bankruptcy.

Another factor that may have an adverse impact on your loan application is whether or not you have outstanding loans with other lenders. **If a bank has seen that you have debt from other lenders, they will be less likely to do business with you.** This can be a problem for small and medium business owners, who typically seek multiple streams of credit with many different loan outlets.

Customer concentrations are another item to be considered in the loan application process. Ideally, you would have a large number of orders from a wide base of customers. Lending institutions might look disfavorably upon large orders from a select few customers. This is because if these customers were to take their business elsewhere, then your business would be affected disproportionately. It is indicative of a centralized business model and a decentralized customer base is generally regarded as being more robust.

# Other Reasons for a Loan Application Rejection

Having an insufficient management team can also serve to hinder a business loan application. Banks will often reject small and medium business enterprises that do not possess strong management skills. There has to be a noticeable chain of command within the organization.  Another thing to remember is that businesses without a checking account have a decreased chance of success.

Lastly, there are a number of concerns that are outside of the control of the business loan applicant. Banks and lending institutions need to make a profit. If the economy takes a bad turn or the industry you are involved in does not have bright prospects for the immediate future, then your application will be refused. This is more likely to be the case with banks as opposed to online lenders.

# Alternative Resources and Financing Options

Aside from getting the standard business term loan from an alternative lender or a bank, there are a number of options available. You could consider some of the loans mentioned above, such as the merchant cash advance, the business line of credit, equipment financing, invoice factoring, and invoice discounting. All of these offer unique benefits that are different from the typical term loans available from lending companies and banks.

**There are many options available  aside from the standard SBA(7)(a) which you could potentially investigate.** These include the small loan program, the community advantage program, of the capline program.

There are also multiple grant programs available in the USA and globally. Getting a loan is great, but getting a grant is even better.  If you are an African American business owner or from a disadvantaged group, then you might be eligible for a loan. The same applies to female applicants. However, it is worth bearing in mind that women and disempowered groups tend to have a harder time obtaining finance. Whether this is due to lending criteria

or cognitive biases is not yet known. Top business grants for women and minorities include:

1. The Eileen Fisher Women-Owned Business Grant Program
2. SBA InnovateHER Challenge
3. Zions Bank Smart Women Grants
4. FedEx Small Business Grant Contest
5. The Amber Grant for Women
6. The Halstead Grant

Another strategy that you might consider is going local. If you are lacking collateral for a long-term business loan, then it is highly unlikely that your loan application is going to be successful. But there are local options available that can increase your chances. Alternatively, there are local peer-to-peer platforms where you can get a loan no matter where you are in the world or what your credit rating happens to be. These platforms can help you to secure a loan easily once you satisfy some basic criteria.

A business credit card is another good way to acquire flexible cash where you only pay interest on when you need. This has an added advantage in that you will be building good credit when using this card to get better loans in the future. You can also benefit from a rewards or points-based system and prioritize aggressive repayments so credit score ratings shoot rapidly upwards.

# The Simple Checklist

While there are many variants of lenders and kinds of loan, there is a simple formula that you can consider to improve a loan application:

1. Understand your credit score and increase it as much as possible.
2. Organize your finances – This means having one business checking account that is separate from everything else.
3. Make sure there is regular and consistent activity where possible.
4. Be diligent with invoicing and financial tracking.
5. Develop a clear map of what you need the money for and how it will be spent.

6. Have a solid business plan.

**The best strategy could be to secure a loan with an alternative lender such as Lending Club or OnDeck. You can take a loan with these lenders for 6 months to a year. In the meantime, you will be building a credit score, increasing your revenue, gathering documentation, and building your case for an SBA(7)(a) loan. It is a good compromise that gives you the best of both worlds.**

The time it takes to prepare, organize, and process a loan from a bank is often not factored into the equation. This is frequently quite stressful. Moreover, time is money, and it may be easier to take a loan with a higher APR and make back the finances in other ways than to undergo a strenuous loan procedure.

# Conclusion

Getting a business loan is vital for the success of any business. Every business owner runs into unforeseen expenses or stumbles across a golden opportunity without the finances to capitalize.

Be proactive with your loan application process right now. Build a strong credit score, increase your annual revenue, and start planning for either an SBA(7)(a) application or an alternative lender. Put simply, the more financially efficient your business is, the lower the rates will be. The flexibility and general conditions of the loan will also be better.

**Remember, you don't have to get the perfect loan starting off. You need to get a good loan now and build for the future so you can get better loans later. The most common trait found among people that understand money is patience. Provided that no mistakes are made, businesses tend to grow and finances tend to gain interest and accrue.**